No. 93-1504

In The

Supreme Court of the United States

October Term, 1993

THE CELOTEX CORPORATION,

Petitioner,

v.

BENNIE EDWARDS and JOANN EDWARDS,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF FOR PETITIONER

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QUESTION PRESENTED FOR REVIEW

Whether Rule 65.1 of the Federal Rules of Civil Procedure allows enforcement of a supersedeas bond, posted to stay execution of judgment against a defendant that filed for reorganization after the judgment became final, against the non-bankrupt surety that issued the bond, even though a bankruptcy court in another circuit has attempted to restrain execution on supersedeas bonds posted in favor of the debtor under section 105(a) of the Bankruptcy Code?

LIST OF PARTIES TO THE PROCEEDING

The parties to the proceeding below are identified in the caption of the case. The Celotex Corporation is wholly-owned by Jim Walter Corporation, and Celotex has a wholly-owned subsidiary, Carey Canada Inc. Although not formally named as a party in the proceeding below, Northbrook Property and Casualty Insurance Company has an interest in the outcome of this case because Northbrook is the surety on the supersedeas bond at issue here.

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BRIEF FOR PETITIONER

Celotex respectfully requests that this Court reverse the judgment of the United States Court of Appeals for the Fifth Circuit, which failed to defer to the injunction issued by the United States Bankruptcy Court for the Middle District of Florida pursuant to 11 U.S.C. §105(a). That injunction stayed respondents Bennie and JoAnn Edwards from collecting their judgment against Celotex by executing upon the supersedeas bond procured by Celotex.

CITATION OF THE OPINIONS AND JUDGMENTS DELIVERED IN THE COURTS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit, permitting the Edwardses to collect their judgment against Celotex by executing upon the supersedeas bond that Celotex posted in the United States District Court for the Northern District of Texas, is reported. *See Edwards v. Armstrong World Indus., Inc.*, 6 F.3d 312 (1993).

After the Fifth Circuit's ruling, Celotex filed a timely petition for rehearing containing a suggestion for rehearing *en banc*. The Fifth Circuit's explanation of why it denied Celotex's rehearing petition is reported. *See Edwards v. Armstrong World Indus., Inc.*, 6 F.3d 321 (1993) (per curiam) (statement on denial of petition for rehearing and suggestion for rehearing *en banc*).

The order of the United States District Court for the Northern District of Texas granting the Edwardses' motion for leave to execute upon Celotex's supersedeas bond is not reported. The text of the order is reproduced in the Appendix to Celotex's Petition for a Writ of Certiorari. *See* App. to Pet. for Cert. 23.

GROUND ON WHICH THIS COURT'S JURISDICTION IS INVOKED

This Court has jurisdiction to review the judgment of the United States Court of Appeals for the Fifth Circuit pursuant to 28 U.S.C. §1254(1).

The Fifth Circuit issued its judgment on November 5, 1993. Thereafter, Celotex filed a timely petition for rehearing containing a suggestion for rehearing *en banc*. The Fifth Circuit denied Celotex's petition for rehearing and refused Celotex's suggestion for rehearing *en banc* on December 22, 1993.

On March 22, 1994, Celotex filed its petition for a writ of certiorari in this Court. This Court granted Celotex's petition for a writ of certiorari on May 23, 1994.

CONSTITUTIONAL PROVISIONS, STATUTES AND FEDERAL RULES INVOLVED

U.S. Const. Art. I, §8, cl. 4: "The Congress shall have Power . . . To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States."

11 U.S.C. §105(a): "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."

11 U.S.C. §510(c): "[A]fter notice and a hearing, the court may – (1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim or all or part of an allowed interest to all or part of another allowed interest; or (2) order that any lien securing such a subordinated claim be transferred to the estate."

28 U.S.C. §157(a): "Each district court may provide that any or all cases under title 11 and any

or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district."

28 U.S.C. §158(a): "The district courts of the United States shall have jurisdiction to hear appeals from final judgments, orders, and decrees, and, with leave of the court, from interlocutory orders and decrees, of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. An appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving."

28 U.S.C. §158(d): "The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees entered under subsections (a) and (b) of this section."

28 U.S.C. §1334(b): "Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11."

28 U.S.C. §2072(a): "The Supreme Court shall have the power to prescribe general rules of practice and procedure . . . for cases in the United States district courts . . . . "

28 U.S.C. §2072(b): "Such rules shall not abridge, enlarge or modify any substantive right. All laws in conflict with such rules shall be of no further force or effect after such rules have taken effect."

Fed. R. Civ. P. 62(d): "When an appeal is taken the appellant by giving a supersedeas bond may obtain a stay. . . . The bond may be given at or

after the time of filing the notice of appeal or of procuring the order allowing the appeal, as the case may be. The stay is effective when the supersedeas bond is approved by the court."

Fed. R. Civ. P. 65.1: "Whenever these rules, including the Supplemental Rules for Certain Admiralty and Maritime Claims, require or permit the giving of security by a party, and security is given in the form of a bond or stipulation or other undertaking with one or more sureties, each surety submits to the jurisdiction of the court and irrevocably appoints the clerk of the court as the surety's agent upon whom any papers affecting the surety's liability on the bond or undertaking may be served. The surety's liability may be enforced on motion without the necessity of an independent action. The motion and such notice of the motion as the court prescribes may be served on the clerk of the court, who shall forthwith mail copies to the sureties if their addresses are known."

Fed. R. Bankr. P. 7004(d): "The summons and complaint and all other process except a subpoena may be served anywhere in the United States."

STATEMENT OF THE CASE

On October 12, 1990, Celotex and its wholly-owned subsidiary, Carey Canada Inc., filed voluntary petitions in bankruptcy for reorganization under Chapter 11 of Title 11, United States Code, in the United States Bankruptcy Court for the Middle District of Florida. *See In re Celotex Corp.*, 128 B.R. 478, 479 (Bankr. M.D. Fla. 1991) (*Celotex I*). Both cases remain pending.

The principal reason why Celotex sought bankruptcy protection was the vast liability that it faced in numerous

bodily injury and property damage suits involving asbestos. Courts have imposed asbestos-related liability upon Celotex as the result of its merger in 1972 with Panacon Corporation, a successor to Philip Carey Corporation. Philip Carey had been a manufacturer of asbestos-containing insulation products.

The question before this Court arises from the interaction, and resulting friction, between the Edwardses' civil tort action against Celotex, instituted in a United States District Court in Texas, and Celotex's bankruptcy case in Florida.

A. The Liability Phase Of The Edwardses' Civil Action

The Edwardses' suit against Celotex illustrates the type of problems that Celotex faced when it filed for relief under the Bankruptcy Code. On August 17, 1987, the Edwardses filed suit in the United States District Court for the Northern District of Texas against Celotex and seventeen other defendants. Jt. App. 1. Bennie Edwards was a former insulation installer who claimed in his complaint to have an asbestos-related injury. *See Edwards v. Armstrong World Indus., Inc.*, 911 F.2d 1151, 1153 (CA5 1990) (*Edwards I*).

In mid-April of 1989, following a five-day trial, the jury returned a verdict in favor of the Edwardses and against Celotex. The jury found that Celotex was liable to the Edwardses for a total of $35,253.80 in compensatory damages.[1] Jt. App. 1. The jury also awarded the Edwardses $245,500.00 in punitive damages. *Id.* The jury

[1] More precisely, the jury awarded Bennie Edwards $10,195.60 in "past damages" and $14,288.20 in "future damages." The jury awarded JoAnn Edwards $3,590.00 in "past damages" and $7,180.00 in "future damages." *See* App. to Pet. for Cert. 24-25.

did so even though Celotex, itself, never sold or manufactured the asbestos-containing products that allegedly caused injury to the Edwardses.

The Texas district court entered judgment on the jury's verdict on April 17, 1989. *Id.* On June 1, 1989, the district court entered an order denying the post-judgment motion that Celotex had filed. Five days later, on June 6, 1989, the district court granted Celotex's motion pursuant to Federal Rule of Civil Procedure 62(d) to provide a supersedeas bond pending appeal. A bond in the amount of $294,987.88 was thereafter provided. Jt. App. 1-2. Northbrook served as surety on the bond. *Id.* Celotex secured its reimbursement obligation to Northbrook (should Northbrook ever be required to pay on the bond) with Celotex's property, in the form of cash payable to Celotex from Northbrook under a settlement agreement resolving insurance coverage disputes. *Edwards v. Armstrong World Indus., Inc.*, 6 F.3d 312, 314 (CA5 1993) (*Edwards II*).

After procuring the supersedeas bond, Celotex appealed from the judgment to the United States Court of Appeals for the Fifth Circuit. Jt. App. 2. On September 20, 1990, the Fifth Circuit affirmed the judgment, expressing misgivings as to the propriety of serial punitive damage awards in mass tort litigation. *Edwards I*, 911 F.2d at 1155. The Fifth Circuit's concerns in this regard were prophetic:

> "Celotex['s] . . . affidavits reflect[ ] that between September, 1988 and March, 1989, judgments for punitive damages exceeding $10 million were entered against it, compared with $15 million in adverse actual damage judgments. If no change occurs in our tort or constitutional law, the time will arrive when Celotex's liability for punitive damages imperils its ability to pay compensatory claims and its corporate existence. Neither the company's innocent shareholders, employees and creditors, nor future asbestos

> claimants will benefit from this death by attrition.
>
> "With our own misgivings, we AFFIRM." *Id.*

Celotex did not file a petition for rehearing of the Fifth Circuit's decision. *Edwards II*, 6 F.3d at 314. As a result, on October 12, 1990, the Fifth Circuit issued its mandate in the tort action. *Id.*

B. The Proceedings In The Bankruptcy Court And The Collection Efforts Of The Edwardses

1. The origins of the 11 U.S.C. §105(a) stay

On October 12, 1990, the time foreseen by the Fifth Circuit in *Edwards I* arrived. On that date, the same day that the Fifth Circuit issued its mandate, Celotex filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code. *See Celotex I*, 128 B.R. at 479.[2]

On October 17, 1990, the Florida bankruptcy court issued an order entitled "Order Granting Emergency Motion for Determination of Applicability of §362 Stay of Pending Matters or, in the Alternative, for Extension of §362 Stay to Pending Matters." App. to Pet. for Cert. 26-29. Relying expressly upon its powers under 11 U.S.C. §105(a), the bankruptcy court decreed in its order:

> "2. All persons (including individuals, partnerships and corporations, and all those acting for or on their behalf), and all governmental units . . . (collectively, 'Entities') be and each of

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[2] Celotex believes the issuance of the mandate on October 12, 1990 occurred before Celotex filed its bankruptcy petition at 3:45 p.m. on that date. The order of these acts, however, is not material to the question presented. The bankruptcy court, without objection by Celotex, would modify the automatic stay under 11 U.S.C. §362(a), as it has consistently done, to permit any necessary conclusion of the *Edwards I* appeal. *See Celotex I*, 128 B.R. at 481 n.9.

them are hereby stayed, restrained and enjoined from:

> " . . .
>
> "f. Taking any act to collect, assess, or recover a claim against any of the Debtors that arose before the commencement of the Chapter 11 cases; . . .
>
> " . . .
>
> "3. Notwithstanding any exceptions or limitations to the automatic stay contained in §362(b) of the code, all entities are hereby jointly and severally stayed, restrained and enjoined from commencing or continuing any judicial, administrative or other proceeding involving any of the Debtors regardless of (a) who initiated the proceeding, (b) whether the matter is on appeal and a supersedeas bond has been posted by the Debtors or (c) the appellant in an appeal is one of the Debtors.
>
> "4. On request of a party in interest, and after not less than thirty (30) days' written notice to the attorneys for the Debtors, and after a hearing, this Court may consider granting relief from the restraints imposed herein in the event that it be deemed necessary, appropriate and warranted to so terminate, annul, modify or condition the injunctive relief granted herein." *In re Celotex Corp.*, Nos. 90-10016-8B1 & 90-10017-8B1 (Bankr. M.D. Fla. 1990) (order dated Oct. 17, 1990) (reprinted in App. to Pet. for Cert. 26-29).

2. The initial efforts to dissolve the §105(a) stay

After the bankruptcy court issued its §105(a) stay, lawyers representing the Edwardses and other asbestos bodily injury creditors appeared in the Florida bankruptcy court to request that the §105(a) stay be lifted to

permit execution upon supersedeas bonds that Celotex had posted. The Edwardses' lawyers argued to the bankruptcy court, in a brief filed on February 28, 1991, that Celotex's supersedeas bonds were not property of Celotex's bankruptcy estate and thus were not subject to the bankruptcy court's control. *See* Jt. App. 35-52 (Memorandum of Counsel for Asbestos-Related Personal Injury Creditors Regarding the Status of Supersedeas Bonds).

The bankruptcy court faced a formidable task in resolving the parties' conflict. The Edwardses and the beneficiaries of over 100 other supersedeas bonds demanded unrestricted payment in full. *Celotex I*, 128 B.R. at 479, 482. Conversely, Celotex, on behalf of unbonded creditors, asserted that there was a need to preserve the status quo with respect to the supersedeas bonds until the bankruptcy court could properly address a number of important debtor-creditor issues directly affecting over 100,000 unbonded creditors with asbestos related claims virtually identical to that of the Edwardses. *Id.* at 479, 482-84. Among the issues to be resolved by the bankruptcy court are: whether some or all of the transfers of assets to procure supersedeas bonds can ultimately be set aside as preferences, *see* 11 U.S.C. §547; whether some or all of the transfers of assets to procure supersedeas bonds can be set aside as fraudulent transfers under state or federal law, *see* 11 U.S.C. §§544, 548; whether some or all of the settlement agreements that Celotex entered into with its insurers, which led to the provision of the supersedeas bonds, can be rejected as executory contracts, *see* 11 U.S.C. §365; and whether some or all of the punitive damage awards returned against Celotex can be subordinated or disallowed, *see* 11 U.S.C. §§510(c), 726(a)(4), 1129(a)(7).[3] *Celotex I*, 128 B.R. at 484.

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[3] The issue of whether bonded punitive damage claims will ultimately be subordinated is particularly significant in this

The significance of these issues to Celotex's creditors, and the bankruptcy case as a whole, cannot be overlooked. If the bonded judgment creditors' interests are not avoided, subordinated or disallowed, this small group, which includes the Edwardses, will collect 100% of their claims, totaling approximately $70,000,000, *Celotex I*, 128 B.R. at 482, including all punitive damages awarded. Accordingly, no portion of this money would be available for asbestos judgment creditors without bonds, known asbestos bodily injury creditors and countless unknown future asbestos bodily injury creditors. These creditors probably will collect only a small fraction of their compensatory claims – and no punitive damages.

The bankruptcy court was required to weigh and balance these competing claims to limited resources. It also had to weigh the effect that allowing immediate execution would have on the successful completion of Celotex's efforts to reorganize its financial affairs, including, *inter alia*, the resolution of insurance coverage disputes with its insurers. Some of these insurers (like Northbrook) were also liable on Celotex's supersedeas bonds and had secured their liability with cash payable from the insurer to Celotex pursuant to settlement agreements. *Id.* at 480. These settlement agreements resolved disputes relating to coverage for asbestos claims under liability policies. This further complicated the bankruptcy court's difficult balancing task.

3. The May 3, 1991 filing of the Edwardses' Rule 65.1 motion in the Texas court

Apparently dissatisfied with how efforts to dissolve the §105(a) stay were proceeding in the Florida bankruptcy court, on May 3, 1991 the Edwardses filed a motion in the

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case. As the Fifth Circuit correctly noted in *Edwards I*, "Celotex's liability for punitive damages imperils its ability to pay compensatory claims." 911 F.2d at 1155.

Texas district court, pursuant to Rule 65.1, seeking to collect their judgment against Celotex by executing upon the supersedeas bond posted by Celotex. Jt. App. 2, 5-8. The Edwardses filed this motion without leave of the bankruptcy court and without awaiting the bankruptcy court's ruling on the efforts to dissolve the §105(a) stay. In the Rule 65.1 motion, the attorneys for the Edwardses made the same argument they had made in the bankruptcy court, namely that Celotex's supersedeas bonds were not property of Celotex's bankruptcy estate and thus were not subject to the bankruptcy court's control. Jt. App. at 5-8. Celotex opposed the Edwardses' motion. *Id.* at 3. Northbrook, as surety, also appeared in the district court and opposed the motion. *Id.* at 2-3, 28-34.

4. The bankruptcy court's June 13, 1991 decision and order regarding the supersedeas bonds

On June 13, 1991, after extensive briefing and oral argument, *Celotex I*, 128 B.R. at 479 n.1., the Florida bankruptcy court issued its opinion and order concerning the supersedeas bonds. The bankruptcy court ruled that judgment creditors who were in the position of the Edwardses – having prevailed on appeal and being the beneficiaries of a supersedeas bond – would not be permitted to execute upon those bonds without first obtaining permission from the bankruptcy court. *Id.* at 484-85. The bankruptcy court decreed:

> "(3) Where at the time of filing the petition, the appellate process between Debtor and the judgment creditor had been concluded, the judgment creditor is precluded from proceeding against any supersedeas bond posted by Debtor without first seeking to vacate the Section 105 stay entered by this Court. It is further
>
> ". . . .

"ORDERED, ADJUDGED AND DECREED the Section 105 stay entered by this Court on October 17, 1990, continues in effect." *Id.* at 485.

In explaining the reasons supporting its ruling, the bankruptcy court commented first upon the §105(a) stay entered on October 17, 1990:

"Upon Debtor's filing its bankruptcy petition, this Court entered an order pursuant to Section 105 which sought to augment the stay protection afforded by Section 362(a). Such order was upon Debtor's motion and was for the purpose of precluding, among other things, judgment creditors from proceeding in various state and federal courts against supersedeas bonds without first coming before this Court." *Celotex I,* 128 B.R. at 482 (footnote omitted).

After reviewing several decisions from various United States Courts of Appeals upholding the use of 11 U.S.C. §105(a) injunctions to stay actions that threatened to impede the reorganization process, *see Celotex I,* 128 B.R. at 483-84, the bankruptcy court wrote:

"These decisions reinforce fundamental bankruptcy policy to stop ongoing litigation and to prevent peripheral court decisions from dealing with issues, properties, or entities involved in a debtor's reorganization process without first allowing the bankruptcy court to have an opportunity to review the potential effect on the debtor. Where bankruptcy courts in 'mega' cases such as this case are required to deal with complex litigation involving numerous parties, joint and several liability, and multi-million dollars in claims and assets, not to mention potential conflicts with other judicial determinations, the powers of the bankruptcy court under Section 105 must in the initial stage be absolute, unless limited by the Bankruptcy Code or other federal laws. Clearly, the role of Section 105 in this type

of case is first to protect the reorganization process." *Id.* at 484.

In concluding its opinion, the bankruptcy court stated:

"As to the utilization of Section 105 vis-a-vis the supersedeas bonds, once the judgment creditor has been successful throughout the appellate process, the judgment creditor is not able to proceed against the supersedeas bond without seeking to vacate the Section 105 stay in this Court. Under these circumstances, it will be Debtor's burden to establish that the Section 105 stay should continue. The Court's inquiry will include Debtor's ability to avoid any final judgment under the Bankruptcy Code and the necessity to protect its sureties or disenfranchise them if such surety agreements can be considered executory contracts or avoided under the avoiding powers in the Bankruptcy Code. (11 U.S.C. §§365, 547, and 548.) Additionally, consideration will be given to Debtor's ability to deal with the targeted litigation within the reorganization plan and the effect on that process if the Section 105 stay is extinguished. The analysis may also include the treatment of those judgments which include punitive damages or joint and several liability or contribution with other asbestos co-defendants. This Court does not seek to establish an exhaustive list of inquiry, as each specter of the Section 105 stay may relate differently to an aspect of Debtor's reorganization process which seeks to be protected." *Id.* (footnote omitted).[4]

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[4] In the omitted footnote, the bankruptcy court addressed the issue of punitive damage awards that had been returned against Celotex:

"Section 726(a)(4) of the Bankruptcy Code provides that punitive damages are fourth in line for distribution in a Chapter

5. The Texas court's May 27, 1992 decision upon the Rule 65.1 motion

After issuance of *Celotex I* on June 13, 1991, Celotex promptly brought that decision and order to the attention of the Texas district court in a supplemental brief. Jt. App. 3, 53-56. Celotex also alerted the Texas district court to the involvement of the Edwardses' counsel in the proceedings leading up to the issuance of the decision and order:

> "Plaintiffs' counsel in this case, the firm of Baron & Budd, P.C., appeared in the proceeding which lead to the entry of the Omnibus Order [*Celotex I*] as one of the counsel for the Asbestos-Related Personal Injury Creditors. As such, the Omnibus Order is binding upon Plaintiffs in this action." Jt. App. 54

Nearly a year later, on May 27, 1992, the Texas district court issued an order, without opinion, granting the Edwardses leave to execute upon the supersedeas bond that Celotex had posted. Jt. App. 3. The order stated, in full:

> "CAME ON TO BE HEARD plaintiffs' Motion for Release of Supersedeas Bond, and the court, being advised of the premises, is of the opinion that said motion has merit and should be granted. It is therefore

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7 liquidation. Although Section 726(a)(4) is inapplicable to Chapter 11 reorganizations (*In re A.H. Robins Co.*, 89 B.R. 555, 560 (E.D. Va. 1988); *In re Alwan Bros.*, 115 B.R. 148, 151 (Bankr. C.D. Ill. 1990)), it is well-established that bankruptcy courts have inherent equitable power to disallow, limit, or subordinate claims for punitive damages in Chapter 11 reorganizations. *In re A.H. Robins Co.*, 89 B.R. at 562; *In re Apex Oil Co.*, 118 B.R. 683, 699 (Bankr. E.D. Mo. 1990); *In re Johns-Manville Corp.*, 68 B.R. 618, 627 (Bankr. S.D.N.Y. 1986), *aff'd*, 78 B.R. 407 (S.D.N.Y. 1987)." *Celotex I*, 128 B.R. at 484 n.12.

> "ORDERED that plaintiffs may execute on the supersedeas bond executed by Northbrook Property and Casualty Insurance Company on May 17, 1989 to secure the judgment entered in plaintiffs' favor against the Celotex Corporation in the above styled and numbered cause." *Edwards v. Celotex Corp.*, No. 7-87-0050 (N.D. Tex. May 27, 1992) (order) (reprinted in App. to Pet. for Cert. 23).

6. The bankruptcy court's May 29, 1992 decision on the subsequent efforts to lift the §105(a) stay

On May 29, 1992, just two days after the date of the Texas district court's order, the Florida bankruptcy court decided motions filed by several other bonded judgment creditors who had prevailed against Celotex on appeal. *In re Celotex Corp.*, 140 B.R. 912 (Bankr. M.D. Fla. 1992) (*Celotex II*). In their motions, these judgment creditors sought relief from the bankruptcy court's §105(a) stay in order to collect their judgments against Celotex. The bankruptcy court held full evidentiary hearings on these motions. Evidence was presented as to, *inter alia*, (a) the financial status of Celotex when the supersedeas bonds were procured, (b) how the supersedeas bonds were procured, (c) the nature of the arrangements and transactions between Celotex and the various sureties, including the transfer of collateral to the sureties to secure Celotex's reimbursement obligations under the supersedeas bonds, (d) the number of bonded asbestos judgments, (e) the number of asbestos claimants who had filed suits prior to those of the bonded asbestos claimants, (f) the available established insurance coverage for asbestos claims and other assets generally available to satisfy unbonded creditors, and (g) the effect on the reorganization effort of allowing execution. *Celotex II*, 140 B.R. at 914.

The bankruptcy court refused to lift the §105(a) stay at that time, reasoning that Celotex would suffer irreparable harm:

> "Debtor, in all instances, has collateralized the supersedeas bonds. The collateral has taken various forms, but one type in particular is illustrative of the linkage associated with irreparable harm. Debtor and many of its insurers on asbestos claims have settled long-ongoing disputes over insurance coverage. Some of these settlement agreements established the maximum amount of insurance coverage, provided for payment to Debtor of these coverage amounts over time, and provided such payments and contract rights could be held by the insurance company as collateral for supersedeas bonds issued on behalf of Debtor in some of the asbestos cases. . . .
>
> "Dissolving the Section 105 stay would merely shift the battleground: if the Section 105 stay were lifted to enable the judgment creditors to reach the sureties, the sureties in turn would seek to lift the Section 105 stay to reach Debtor's collateral, with corresponding actions by Debtor to preserve its rights under the settlement agreements. Such a scenario could completely destroy any chance of resolving the prolonged insurance coverage disputes currently being adjudicated in this Court. The settlement of the insurance coverage disputes with all of Debtor's insurers may well be the linchpin of Debtor's formulation of a feasible plan. Absent the confirmation of a feasible plan, Debtor may be liquidated or cease to exist after a carrion feast by the victors in a race to the courthouse." *Celotex II*, 140 B.R. at 914-15 (footnote omitted).

In denying the motions of these judgment creditors for leave to execute upon Celotex's supersedeas bonds,

the bankruptcy court again balanced the competing interests of the bonded judgment creditors, such as the Edwardses, with the interests of unbonded asbestos bodily injury claimants. *Id.* at 915-17.

To maintain the status quo, the bankruptcy court directed Celotex to establish a reserve account to ensure that, in the event Celotex was unsuccessful in efforts to recover the assets related to the supersedeas bonds, the bonded judgment creditor plaintiffs, such as the Edwardses, would not be harmed either by a depletion of estate assets or by delay in execution against the sureties. *Id.* at 917. Celotex has complied with the bankruptcy court's order to provide this additional protection.

The bankruptcy court also directed Celotex to file "any preference action or any fraudulent transfer action or any other action to avoid or subordinate any judgment creditor's claim against any judgment creditor or against any surety within 60 days of the entry of this Order." *Id.* Celotex filed such an action in the bankruptcy court against the Edwardses, 227 similarly situated bonded judgment creditors in over 100 cases and the entities from which Celotex procured its supersedeas bonds. *See Celotex, et al. v. Allstate Ins. Co., et al.*, Adversary No. 92-584 (Bankr. M.D. Fla.). This proceeding is pending and will resolve the avoidance, subordination and disallowance issues which necessitated the §105(a) stay – unless that process is mooted by collection of judgments against Celotex by execution on the supersedeas bonds in violation of the stay.

7. The appeal from the Texas court's order granting the Rule 65.1 motion

On June 26, 1992, Celotex filed a notice of appeal to the United States Court of Appeals for the Fifth Circuit

from the Texas district court's May 27, 1992 order allowing the Edwardses to execute upon Celotex's supersedeas bond. Jt. App. 3-4, 64-65.

On November 5, 1993, the Fifth Circuit affirmed. *Edwards II*, 6 F.3d 312. The Fifth Circuit saw its task on appeal as follows:

> "It is this Court's duty to insure that the case management tools the bankruptcy court utilizes to control these conflicts do not overwhelm its primary obligation to dispense justice." *Id.* at 314.

The court began by examining whether the Texas district court had jurisdiction to determine the "applicability" of the bankruptcy court's stay. *Id.* at 315. The Fifth Circuit answered this question in the affirmative. *Id.* at 315-16.[5] The Fifth Circuit subsequently addressed what it described as "the more difficult issue raised by this appeal," "whether the equitable powers granted bankruptcy courts apply to the type of non-debtor third parties present here." *Id.* at 317.

The court proceeded to engage in a lengthy analysis of the merits of the bankruptcy court's §105(a) injunction. *See* 6 F.3d at 317-20. It recognized that "[s]ection 105 authorizes a bankruptcy court to enjoin litigants from pursuing actions pending in other courts that threaten the integrity of a bankrupt's estate." *Id.* at 320. Nevertheless, the Fifth Circuit disagreed with the merits of the particular §105(a) stay at issue, holding that "the integrity of the estate is not implicated in the present case because the debtor has no present or future interest in this supersedeas bond." 6 F.3d at 320 (footnote omitted).

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[5] The Fifth Circuit also considered whether the automatic stay, 11 U.S.C. §362, prohibited the Edwardses from executing upon Celotex's supersedeas bond. The Fifth Circuit held that the automatic stay did not bar execution. *Edwards II*, 6 F.3d at 316-17.

In explaining further its reasons for refusing to defer to the bankruptcy court's §105(a) injunction, the Fifth Circuit wrote:

> "The Edwards were specifically promised by the court and by Celotex that they could look to the supersedeas bonds if they won on appeal and we should be careful to see that their expectations are not nullified because of a generalized and theoretical concern for the bankrupt's estate." 6 F.3d at 320.

Accordingly, the Fifth Circuit affirmed the district court's order permitting the Edwardses to execute on Celotex's supersedeas bond – despite the bankruptcy court's §105(a) injunction barring the Edwardses from doing just that.

Thereafter, Celotex filed a petition for rehearing and a suggestion for rehearing *en banc* in the Fifth Circuit. Jt. App. 4. In a published per curiam opinion denying Celotex's rehearing petition, the Fifth Circuit wrote:

> "Appellants contend that we should not collaterally attack an order of a bankruptcy court sitting under the jurisdiction of the Eleventh Circuit. This contention fails for two reasons. Primarily, the bankruptcy court's order does not purport to reach the proceedings in this case and therefore executing the supersedeas bond does not infringe on the Eleventh Circuit's proper jurisdiction. Secondarily, our opinion merely declares this court's power to protect and preserve supersedeas bonds posted in our district courts. Thus, we have not held that the bankruptcy court in Florida was necessarily wrong; we have only concluded that the district court, over which we do have jurisdiction, was right." 6 F.3d at 321 (per curiam) (statement on denial of petition for rehearing and suggestion for rehearing *en banc*).

On March 22, 1994, Celotex filed a petition for a writ of certiorari seeking review of the Fifth Circuit's ruling in

Edwards II. The petition explained that the Fifth Circuit's decision in *Edwards II*, refusing deference to the Florida bankruptcy court's order, was in direct conflict with the decision of the United States Court of Appeals for the Fourth Circuit in *Willis v. Celotex Corp.*, 978 F.2d 146 (1992), *cert. denied*, 113 S. Ct. 1846 (1993).

In *Willis*, the Fourth Circuit vacated an order of the United States District Court for the Eastern District of Virginia which had permitted execution upon a supersedeas bond posted by Celotex. *Id.* at 150. The Fourth Circuit directed Celotex's bonded judgment creditors to seek permission to execute on Celotex's supersedeas bond from the Florida bankruptcy court as required by the bankruptcy court's §105(a) stay. *Willis*, 978 F.2d at 149-50.

On May 23, 1994, this Court granted Celotex's petition for a writ of certiorari. Jt. App. 66.

SUMMARY OF THE ARGUMENT

The judgment of the United States Court of Appeals for the Fifth Circuit should be reversed.

This Court has repeatedly held that persons who are subject to the commands of an injunctive order must obey those commands unless and until the order is modified by the issuing court or reversed on appeal therefrom, notwithstanding the existence of eminently reasonable and proper objections to the merits of the order.

Here, the Fifth Circuit utterly disregarded these holdings when it permitted respondents Bennie and JoAnn Edwards to prevail in their Rule 65.1 motion filed in the United States District Court for the Northern District of Texas. That motion constituted a collateral attack upon the interim 11 U.S.C. §105(a) injunction issued by the United States Bankruptcy Court for the Middle District of Florida staying collection of judgments against Celotex

by execution against Celotex's supersedeas bonds in courts throughout the nation.

In enacting 11 U.S.C. §105(a), Congress expressly granted bankruptcy courts the power to issue injunctions where necessary or appropriate. Once Celotex filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code in the Middle District of Florida, the bankruptcy court in that district had subject matter jurisdiction to issue §105(a) injunctions deemed necessary or appropriate to protect Celotex's reorganization and the property of Celotex's bankruptcy estate.

The particular §105(a) injunction at issue prohibits the Edwardses from collecting their judgment against Celotex by executing upon Celotex's supersedeas bond. The Edwardses are not without recourse, however, as the supersedeas bond remains on file, intact, in the Texas district court. Moreover, the Edwardses and other similarly situated judgment creditors may seek relief from the §105(a) injunction in the Florida bankruptcy court.

Under the circumstances, both the Texas district court and the Fifth Circuit departed radically from the accepted and usual course of judicial proceedings when they reviewed the merits of the Florida bankruptcy court's §105(a) injunction and, believing the injunction to lack merit, permitted the Edwardses to disobey the injunction. Instead, the Texas district court and the Fifth Circuit should have instructed the Edwardses to seek relief from the §105(a) injunction in the bankruptcy court. Only the Florida bankruptcy court and the courts to which appeals may be taken therefrom are empowered to pass upon the necessity and propriety of the particular §105(a) injunction at issue, lest chaos be invited.

Federal Rule of Civil Procedure 65.1 does not, and indeed cannot, authorize the Texas district court to permit the Edwardses to violate the Florida bankruptcy court's binding §105(a) injunction. Rule 65.1, which

merely provides a streamlined procedure by which judgment creditors may recover against sureties, cannot be read to allow recovery against a surety where such recovery is prohibited by an injunction issued by another federal court. Rule 65.1 does not permit a district court, presented with a collateral attack, to override the injunction-issuing authority that Congress vested in the bankruptcy courts when it enacted 11 U.S.C. §105(a). Indeed, Rule 65.1 only answers the question of how, not if or when, a judgment creditor may recover against a surety bond. The Edwardses may properly resort to Rule 65.1 if the Florida bankruptcy court permits them to execute upon Celotex's supersedeas bond.

The record before the Texas district court and the Fifth Circuit was, as is typically the case in a collateral attack, inadequate to allow an informed decision on the merits. However, if this Court determines it is appropriate to review the §105(a) order on its merits by means of this collateral attack, this Court should conclude that the bankruptcy court did not abuse its discretion in issuing the §105(a) stay.

The bankruptcy court acted within its jurisdiction and discretion in determining that Celotex's reorganization would be substantially impeded if judgment creditors such as the Edwardses were permitted to recover against surety bonds, secured by property of Celotex's bankruptcy estate, without first obtaining permission from the bankruptcy court.

For these reasons, the judgment of the United States Court of Appeals for the Fifth Circuit should be reversed.

ARGUMENT

I. THE FIFTH CIRCUIT ERRED IN ALLOWING THE EDWARDSES TO SUCCEED IN A COLLATERAL ATTACK UPON THE BANKRUPTCY COURT'S 11 U.S.C. §105(a) INJUNCTION

A. The Fifth Circuit Should Have Required The Edwardses To Pursue Their Remedies In The Bankruptcy Court

1. Injunctions may not be collaterally attacked except in certain rare instances, none of which is suggested on this record and none of which was found to exist by either the Texas court or the Fifth Circuit

The Florida bankruptcy court's 11 U.S.C. §105(a) injunction stayed the Edwardses and all other similarly situated judgment creditors from collecting their judgments against Celotex by execution upon Celotex's supersedeas bonds. The Edwardses agree that the injunction "was intended to, and did, enjoin collection attempts like those made by the Edwards against Northbrook in this case." Brief in Opposition at 6 n.2. It is also undisputed that when the Texas district court permitted the Edwardses to execute upon Celotex's supersedeas bond, the court allowed them to succeed in a collateral attack upon the §105(a) injunction issued by the bankruptcy court. *See* Brief in Opposition at 6 ("The Edwards agree with Petitioners Celotex and Northbrook that the Fifth Circuit's decision in this case upholds a collateral attack on a stay order issued by a bankruptcy judge in another circuit.").

This Court has repeatedly held that injunctive orders are not subject to collateral attack except in certain limited instances, none of which is even suggested in this case. In *GTE Sylvania, Inc. v. Consumers Union of United States, Inc.*, 445 U.S. 375, 386 (1980), this Court reiterated

"the established doctrine that persons subject to an injunctive order issued by a court with jurisdiction are expected to obey that decree until it is modified or reversed, even if they have proper grounds to object to the order." *See also Howat v. Kansas*, 258 U.S. 181, 189-90 (1922).

In *Pasadena City Bd. of Educ. v. Spangler*, 427 U.S. 424, 439-40 (1976), this Court stated that "those who are subject to the commands of an injunctive order must obey those commands, notwithstanding eminently reasonable and proper objections to the order, until it is modified or reversed." The Florida bankruptcy court's §105(a) injunction staying execution upon supersedeas bonds provided by Celotex has not been modified or reversed, yet neither the Fifth Circuit nor the Texas district court required the Edwardses to abide by the terms of the stay.

This Court has specifically applied the general prohibition against collateral attacks to the orders of federal courts exercising bankruptcy jurisdiction.

In *Steelman v. All Continent Corp.*, 301 U.S. 278 (1937), a unanimous Court, speaking through Justice Cardozo, held that an injunction issued pursuant to §2a(15) of the former Bankruptcy Act properly precluded the institution and maintenance in another forum of a separate civil action that would impair the conduct of the bankruptcy case and the jurisdiction of the bankruptcy court. This Court in *Steelman* thus upheld the bankruptcy court's §2a(15) injunction in the face of a collateral attack. Section 2a(15) of the Bankruptcy Act was the predecessor of §105(a) of the Bankruptcy Code.[6] If injunctions issued

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[6] In §105(a) of the Bankruptcy Code, Congress conferred upon bankruptcy courts even broader power than had been conferred under §2a(15) of the Bankruptcy Act:

"Section 105 is much broader than Section 2a(15), and constitutes a major departure from that law in that it is in no way circumscribed by possession or custody of a *res*. Unlike the restriction under prior law that an order of a bankruptcy court must be '*necessary* for the enforcement of the provisions of this title,' section 105 authorizes the bankruptcy court to also issue orders '*appropriate* to carry out the provisions of this title.' This change evidences Congress' intent that bankruptcy courts would, under the Bankruptcy Code, deal with all phases and aspects of a bankruptcy case." 2 *Collier on Bankruptcy* ¶105.01[2], at 105-3 to 105-4 (Lawrence P. King ed., 1994) (emphasis in original; footnote omitted).

pursuant to §2a(15) of the Bankruptcy Act were immune from collateral attack, it follows that injunctions issued pursuant to §105(a) of the Bankruptcy Code are similarly immune.

Likewise rebuffing a collateral attack upon a bankruptcy court's order, in *Chicot County Drainage Dist. v. Baxter State Bank*, 308 U.S. 371 (1940), this Court held:

> "The argument is pressed that the District Court was sitting as a court of bankruptcy, with the limited jurisdiction conferred by statute, and that, as the statute was later declared to be invalid, the District Court was without jurisdiction to entertain the proceeding and hence its decree is open to collateral attack. We think the argument untenable. The lower federal courts are all courts of limited jurisdiction, that is, with only the jurisdiction which Congress has prescribed. But none the less they are courts with authority, when parties are brought before them in accordance with the requirements of due process, to determine whether or not they have jurisdiction to entertain the cause and for this purpose to construe and apply the statute under which they are asked to act. Their determinations of such questions, while open to direct review, may not be assailed collaterally." *Id.* at 376.

This Court has recognized three exceptions to the rule that one who is bound by an injunctive order may not collaterally attack the order but instead must seek to have the order revised or vacated either in the issuing court or on appeal. *See Walker v. City of Birmingham*, 388 U.S. 307, 315 (1967) (noting exceptions). Neither the Texas district court nor the Fifth Circuit found facts or circumstances permitting the invocation of any of these exceptions.

The first exception arises where the issuing court lacked subject matter jurisdiction. *See GTE Sylvania*, 445 U.S. at 386 (rebuffing collateral attack against "an injunctive order issued by a court with jurisdiction"); *Walker*, 388 U.S. at 315 (injunction may not be collaterally attacked when issued by a court with "jurisdiction . . . over the subject matter of the controversy").

The second exception arises where the court that issued the injunction lacked personal jurisdiction over the parties sought to be enjoined. *See Walker*, 388 U.S. at 315 (injunction may not be collaterally attacked when issued by a court with "jurisdiction over the petitioners"); *see also Insurance Corp. of Ireland, Ltd. v. Compagnie des Bauxites de Guinee*, 456 U.S. 694, 711 n.1 (1982) (Powell, J., concurring in the judgment) ("A district court must have personal jurisdiction over a party before it can enjoin its actions.").

The third exception arises where "the injunction was transparently invalid or had only a frivolous pretense to validity." *Walker*, 388 U.S. at 315.

Celotex now. turns to demonstrate that the Edwardses cannot claim the benefit of any of these three exceptions to the rule prohibiting collateral attacks upon injunctive orders.

2. None of the three recognized exceptions to the prohibition on collateral attack is present

a. The first exception is inapplicable because the bankruptcy court had subject matter jurisdiction to issue injunctions pursuant to 11 U.S.C. §105(a) in Celotex's bankruptcy proceeding

In *United States v. Morton*, 467 U.S. 822, 828 (1984), this Court explained that "[s]ubject-matter jurisdiction defines the court's authority to hear a given type of case. . . . " Celotex filed a voluntary petition for reorganization under Chapter 11 of the Bankruptcy Code on October 12, 1990 in the Middle District of Florida. As authorized under 28 U.S.C. §§157 and 1334, the United States District Court for the Middle District of Florida has referred its exclusive jurisdiction over all bankruptcy cases, including Celotex's bankruptcy case, to the United States Bankruptcy Court for the Middle District of Florida.

As a result, the Florida bankruptcy court's subject matter jurisdiction over Celotex's bankruptcy proceeding cannot be disputed.

Nor can it be suggested that the issuance of injunctive relief is beyond the power of a bankruptcy court.[7]

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[7] The Edwardses have suggested that the question of the bankruptcy court's "power" to issue its §105(a) stay implicates the bankruptcy court's subject matter jurisdiction. *See* Brief in Opposition at 9. Celotex therefore discusses the bankruptcy court's power at this point.

However, this Court has recognized, in a case arising under patent law, that a challenge to a court's power to issue an injunction does not constitute a challenge to the issuing court's subject matter jurisdiction. *See The Fair v. Kohler Die & Specialty Co.*, 228 U.S. 22, 23-26 (1913) (Holmes, J.). Rather, this Court held that the challenge to the issuing court's power constituted an

This Court has observed on numerous occasions that bankruptcy courts are courts of equity with power to enjoin actions that would undermine the due administration of a bankruptcy estate and the preservation of the rights of both secured and unsecured creditors. *See, e.g., Isaacs v. Hobbs Tie & Timber Co.*, 282 U.S. 734 (1931) (exercise of power to ascertain the validity of liens, marshal them, control their enforcement and liquidation); *Local Loan Co. v. Hunt*, 292 U.S. 234 (1934) (exercise of power to enjoin attempt to enforce claim under wage assignment); *Pepper v. Litton*, 308 U.S. 295 (1939) (exercise of broad equitable power to subordinate or disallow claim reduced to judgment); *Young v. Higbee Co.*, 324 U.S. 204, 214 (1945) ("exercise [of] all equitable powers unless prohibited by the Bankruptcy Act" to order an accounting of improper benefits); *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 527 (1984) (exercise of power as "a court of equity" to determine how the equities of rejecting a collective bargaining agreement relate to the success of a reorganization).

This Court need not rely exclusively upon the general inherent equitable powers of bankruptcy courts to conclude that the Florida bankruptcy court had the power to issue injunctions; Congress specifically gave bankruptcy courts the power to issue injunctions of the type at issue when it enacted 11 U.S.C. §105(a).

Section 105(a) provides that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." In *United States v. Energy Resources Co.*, 495 U.S. 545 (1990), this Court explained:

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attack upon the merits of the injunction. *See id.* at 26; *see also United States v. Holtzman*, 762 F.2d 720, 724 (CA9 1985) ("federal courts do not depend upon a specific delegation of power to issue injunctions in cases over which they otherwise have subject matter jurisdiction").

> "The Code also states that bankruptcy courts may 'issue any order, process, or judgment that is necessary or appropriate to carry out the provisions' of the Code. §105(a). These statutory directives are consistent with the traditional understanding that bankruptcy courts, as courts of equity, have broad authority to modify creditor-debtor relationships." *Id.* at 549.

The legislative history of §105(a) confirms that the Florida bankruptcy court was not acting beyond its power in issuing the injunction that is the subject of the Edwardses' collateral attack:

> *"The court has ample other powers to stay actions not covered by the automatic stay.* Section 105, of proposed Title 11, derived from Bankruptcy Act §2a(15), grants the power to issue orders necessary or appropriate to carry out the provisions of title 11." S. Rep. No. 989, 95th Cong., 2d Sess. 51 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5837 (emphasis added).

See also H.R. Rep. No. 595, 95th Cong., 2d Sess. 342 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6298 (containing identical text).

The conclusion that the Florida bankruptcy court was well within its power when it issued an injunction pursuant to §105(a) gains further support from this Court's decisions construing §105(a)'s predecessor, §2a(15) of the Bankruptcy Act. For example, in *Steelman*, 301 U.S. at 289-91, this Court held that the bankruptcy court properly used §2a(15) to enjoin a corporation controlled by the debtor from initiating and maintaining a suit in another forum that threatened to undermine the bankruptcy court's ability to prevent the debtor from consummating a fraud upon his creditors.

Similarly, in *Continental Ill. Nat'l Bank & Trust Co. v. Chicago, R.I. & P. Ry. Co.*, 294 U.S. 648 (1935), this Court held:

"Moreover, by §2(15) of the Bankruptcy Act (U.S.C., Title 11, §11), courts of bankruptcy are invested with such authority in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings, including the power to 'make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this act.'. . . .

"The bankruptcy court, in granting the injunction, was well within its power, either as a virtual court of equity, or under the broad provisions of §2(15) of the Bankruptcy Act or §262 of the Judicial Code." *Id.* at 676.

For these reasons, it is beyond question that the Florida bankruptcy court had subject matter jurisdiction over Celotex's reorganization. The bankruptcy court also had the power, expressly granted by Congress in 11 U.S.C. §105(a) and inherent in a court of equity, to issue injunctive orders. The Edwardses thus fail to come within the first of the three limited exceptions to the rule that injunctive orders may not be collaterally attacked.

b. The second exception is inapplicable because the bankruptcy court had personal jurisdiction over the Edwardses

Counsel for the Edwardses actively participated before the bankruptcy court in briefing the issues of whether the bankruptcy court could and should continue its stay of execution upon Celotex's supersedeas bonds.[8]

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[8] Having actually participated through counsel in the §105(a) litigation that occurred in the bankruptcy court, the Edwardses' collateral attack constitutes a particular affront to the established means by which a dissatisfied party may seek further review of an order. *See Stoll v. Gottlieb*, 305 U.S. 165 (1938) (holding that orders of bankruptcy court are entitled to preclusive effect when subject to collateral attack). The Edwardses' participation through counsel in the bankruptcy court proceedings distinguishes this case from *Martin v. Wilks*, 490 U.S. 755, 761-69 (1989), where this Court held that those who were neither parties to nor participants in an action could not be bound by the terms of a consent decree reached in the action. The Edwardses' reliance upon *Martin* for the proposition that collateral attacks are routinely condoned, *see* Brief in Opposition at 7, is misplaced.

However, even if the Edwardses' counsel had not appeared and participated on behalf of the Edwardses' interests in the proceedings before the bankruptcy court, that court nevertheless had personal jurisdiction over them. Section 1334 of Title 28, United States Code, confers federal question jurisdiction over proceedings in bankruptcy. Bankruptcy Rules 7004(d) and 9014 invest bankruptcy courts with nationwide service of process.[9]

The relevant inquiry to determine whether the Florida bankruptcy court had personal jurisdiction over the Edwardses even if they had not appeared and participated in the bankruptcy proceedings is thus whether the Edwardses had sufficient minimum contacts with the United States. *See Diamond Mortgage Corp. v. Sugar*, 913 F.2d 1233, 1242-44 (CA7 1990), *cert. denied*, 498 U.S. 1089 (1991); *see also United Elec., Radio & Mach. Workers of Am. v. 163 Pleasant St. Corp.*, 960 F.2d 1080, 1085 (CA1 1992) (in federal question cases in which a court enjoys nationwide service of process, "the Constitution requires only that the defendant have the requisite 'minimum contacts' with

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[9] Bankruptcy Rule 7004(d) provides that "[t]he summons and complaint and all other process except a subpoena may be served anywhere in the United States." Bankruptcy Rule 9014 makes this nationwide service of process provision applicable in the context of contested matters (such as the various §105(a) proceedings).

the United States, rather than with the particular forum state").

As the Second Circuit explained in *Mariash v. Morrill*, 496 F.2d 1138 (1974), when examining another federal statute providing for nationwide service of process: "where, as here, the defendants reside within the territorial boundaries of the United States, the 'minimal contacts' required to justify the federal government's exercise of power over them are present." *Id.* at 1143 (footnote omitted). *See also Lisak v. Mercantile Bancorp, Inc.*, 834 F.2d 668, 671 (CA7 1987) (Easterbrook, J.) (holding in a RICO suit that an Illinois district court properly exercised personal jurisdiction over Florida resident who had no contacts with Illinois and noting that defendant "may not demand that the court applying the law of the United States be conveniently located"), *cert. denied*, 485 U.S. 1007 (1988).

It is undisputed that the Edwardses reside within the United States and had notice of the bankruptcy court's injunction. *See Celotex I*, 128 B.R. at 478 (list of counsel showing the participation of the Edwardses' counsel); Jt. App. 55-56 (certificate of service).

For these reasons, the Florida bankruptcy court possessed personal jurisdiction over the Edwardses. Accordingly, the second of the three limited exceptions to the rule prohibiting collateral attacks upon injunctive orders is unavailable to the Edwardses.

c. The third exception is inapplicable because the bankruptcy court's §105(a) stay was neither transparently invalid nor did it have only a frivolous pretense to validity

The §105(a) injunction at issue here is far removed from the type of frivolous injunction that this Court in *Walker* contemplated could be collaterally attacked. The

Fourth Circuit has already held that the §105(a) injunction is deserving of deference. *See Willis*, 978 F.2d at 149-50. In *Willis*, the Fourth Circuit held:

> "We agree with the bankruptcy court that immediate execution against sureties on supersedeas bonds would have been detrimental to Celotex's ability to formulate a plan of reorganization. A hiatus from execution on the bonds was necessary to permit the bankruptcy court to take control of the immense litigation and to examine the underlying tort judgments to establish whether any portion of the awards was voidable. Consequently, the bankruptcy court did not act improperly in enjoining execution on supersedeas bonds posted to secure judgments against Celotex under §105(a)." *Id.* at 150.

If the Fourth Circuit's decision in *Willis* were not sufficient to prove the point, numerous other courts of appeals have held that a bankruptcy court may use 11 U.S.C. §105(a) to enjoin a creditor from proceeding against a third-party, just as the Florida bankruptcy court did when it enjoined Celotex's judgment creditors from proceeding against Celotex's sureties.

For example, in *MacArthur Co. v. Johns-Manville Corp.*, 837 F.2d 89 (CA2), *cert. denied*, 488 U.S. 868 (1988), the Second Circuit affirmed the bankruptcy court's issuance of a §105(a) injunction barring creditors from proceeding directly against the debtor's products liability insurers, explaining:

> "Additional authority for the injunction is to be found in section 105(a) of the Bankruptcy Code, which permits the Bankruptcy Court to 'issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.' This provision has been construed liberally to enjoin suits that might impede the reorganization process. In this case, the Bankruptcy Court found as a fact that to permit actions

> against Manville's insurers arising from Manville's policies would adversely affect property of the estate and would interfere with reorganization." 837 F.2d at 93 (citations omitted).

In *Oberg v. Aetna Casualty & Sur. Co. (In re A.H. Robins Co.)*, 828 F.2d 1023, 1024-26 (CA4 1987), *cert. denied*, 485 U.S. 969 (1988), the Fourth Circuit affirmed a bankruptcy court's §105(a) injunction barring products liability plaintiffs from bringing direct actions against the debtor's insurers even though it was assumed that the plaintiffs, if successful on their claims, would not recover any property of the debtor's estate.

Similarly, in *In re Davis*, 730 F.2d 176 (CA5 1984) (per curiam), the Fifth Circuit itself recognized the breadth of §105(a):

> "under 11 U.S.C. §105(a) a bankruptcy court is authorized, once jurisdiction is established, to 'issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.' This provision includes the authority to enjoin litigants from pursuing actions pending in other courts that threaten the integrity of a bankrupt's estate." 730 F.2d at 183-84 (footnote omitted).

While the particular 11 U.S.C. §105(a) stay that the Florida bankruptcy court issued as to supersedeas bonds was predicated upon unique factual circumstances and may be the subject of disagreement,[10] the foregoing decisions, and numerous others upholding the use of 11 U.S.C. §105(a) in circumstances similar to those facing the

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[10] *Compare Celotex I*, 128 B.R. at 484, *with Keene Corp. v. Acstar Ins. Co. (In re Keene Corp.)*, 162 B.R. 935, 944-49 (Bankr. S.D.N.Y. 1994).

Florida bankruptcy court,[11] demonstrate that the Edwardses cannot establish that the bankruptcy court's §105(a) injunction was either "transparently invalid" or had "only a frivolous pretense to validity." *Walker*, 388 U.S. at 315. Hence, the third exception allowing collateral attack is unavailable.

In sum, there is no record below that would permit the Edwardses to establish facts or circumstances that would allow application of any of the three narrow exceptions to the rule prohibiting collateral attacks upon injunctive orders. Accordingly, the Fifth Circuit erred in permitting the Edwardses to execute upon Celotex's supersedeas bond in violation of the bankruptcy court's §105(a) stay.[12]

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[11] *See, e.g., LTV Corp. v. Miller (In re Chateaugay Corp.)*, 109 B.R. 613 (S.D.N.Y. 1990), *appeal dismissed*, 924 F.2d 480 (CA2 1991):

"The power of the Bankruptcy Court to enjoin the prosecution of suits which threaten the integrity of the reorganization process is not dependent on a showing that direct liability is sought to be imposed on the debtor. On the contrary, such an order is in the nature of an in rem injunction, in which the res, the reorganization, is protected in order to preserve the integrity of the bankruptcy court's necessarily exclusive jurisdiction." *Id.* at 622 (citations omitted).

[12] Celotex does not dispute that both the Texas district court and the Fifth Circuit could conduct a limited inquiry into whether the §105(a) injunction truly was an order of the court and whether Celotex had actually filed for bankruptcy. It should have quickly become evident to the district court and the Fifth Circuit that the Florida bankruptcy court had subject matter jurisdiction to issue the §105(a) injunction and that the Edwardses were not asserting any other ground that would permit a collateral attack. Thus, the Texas district court and the Fifth Circuit should have refrained from reaching both the merits of the Edwardses' motion seeking to execute upon the supersedeas bond and the merits of the bankruptcy court's §105(a) injunctive order.

3. Affirmance of the Fifth Circuit's ruling will produce chaos

This Court should not overlook the destructive consequences to our federal judicial system that will result if the Fifth Circuit's permissive view of collateral attack were to be upheld. The bankruptcy clause of the Constitution, giving Congress authority to establish "uniform Laws on the subject of Bankruptcies throughout the United States," U.S. Const. Art. I, §8, cl. 4, would be rendered a nullity. If this Court were to affirm the Fifth Circuit's judgment, §105(a) injunctions would achieve nationwide effect only in those rare instances where every other federal and state court in the land agreed with the issuing court's weighing of the equities giving rise to the injunction.

Moreover, if the Fifth Circuit's permissive approach to a collateral attack were to be affirmed, judicial administration and the orderly process of judicial review will be undermined. All federal courts would be free to collaterally attack and second-guess the orders of all other such courts – simply because the deciding court disagrees with the merits of the other court's ruling. This will encourage forays to other forums, a multiplicity of proceedings, expense, delay and procedural maneuvering, thereby completely disrupting judicial administration and destroying confidence in the legal process. The ultimate result will be uncertainty and inconsistency in the law, increasing the number of directly conflicting rulings by coordinate federal courts and generating additional appeals to resolve the conflicts. It may even require this Court to intervene (through certiorari) more often, simply to settle such conflicts. In short, affirmance will produce conflict and chaos. This should not and cannot be countenanced.

For all of these reasons, the courts below erred – on both legal and policy grounds – when they permitted the

Edwardses to succeed in their collateral attack. Accordingly, the judgment of the Fifth Circuit should be reversed.

II. FEDERAL RULE OF CIVIL PROCEDURE 65.1 DOES NOT PERMIT THE TEXAS COURT TO ALLOW THE EDWARDSES TO VIOLATE THE TERMS OF THE §105(a) INJUNCTION

A. Nothing In Rule 65.1, Providing A Streamlined Procedure For Judgment Creditors To Recover Against Sureties, Allows Recovery Against A Surety Where Prohibited By A Stay

In this case, the Edwardses elected to use Rule 65.1 as the means to collect their judgment. Rule 65.1 affords judgment creditors two procedural advantages: (1) judgment creditors need not initiate a separate lawsuit against the surety to recover on the bond; and (2) the clerk of the district court where the bond was provided will accept service of the motion seeking execution upon the bond on the surety's behalf. *See* Fed. R. Civ. P. 65.1. The rule thus "permits the liability of a surety to be enforced through an expeditious, summary procedure. . . . " *United States v. Lacey*, 982 F.2d 410, 413 n.2 (CA10 1992) (internal quotations and citation omitted).

Any attempt to collect the judgment would have been a violation of the §105(a) stay, as the Edwardses concede. *See* Brief in Opposition at 6 n.2. Thus, it is irrelevant whether the Edwardses used Rule 65.1, sued Northbrook on the bond in a separate action in Illinois, where Northbrook is located, or sued Northbrook on the bond in a separate action in the Texas district court.

Put simply, Rule 65.1 does not entitle the Edwardses to a different and better substantive outcome than if they had initiated a separate civil suit against Northbrook in Illinois or Texas to execute upon the bond. Rule 65.1

contains no grant of authority which permits a district court to override the injunction-issuing power that Congress vested in bankruptcy courts when it enacted 11 U.S.C. §105(a).

Although Rule 65.1 explains how a party may execute upon a supersedeas bond, the rule is silent concerning if and when a party may so execute. Thus, a district court presented with a Rule 65.1 motion must necessarily first inquire into whether execution is lawfully permitted at the time execution is sought. For example, if execution is being sought too soon – either before a judgment is affirmed on appeal or before the court of appeals returns its mandate to the district court – the Rule 65.1 motion must be denied. Of necessity, a district court's ruling on a Rule 65.1 motion must be governed by the determination of whether execution upon the supersedeas bond is otherwise permitted at the time execution is being sought. Thus, the §105(a) stay should have been dispositive of the Edwardses' Rule 65.1 motion in the Texas district court.

Nearly one year before the Texas district court decided the Rule 65.1 motion that the Edwardses filed in that court, the Florida bankruptcy court made clear that the Edwardses were stayed from executing upon Celotex's supersedeas bond. Two days after the Texas district court issued its order granting the Edwardses' Rule 65.1 motion, the Florida bankruptcy court reaffirmed the continued need for and propriety of its §105(a) injunction. At the time the Texas district court decided the Edwardses' Rule 65.1 motion, it was plain that existing law did not allow execution upon the supersedeas bond. The Texas district court therefore should have denied the Edwardses' Rule 65.1 motion.

B. Rule 65.1 May Not Impair Substantive Rights Protected Under The Bankruptcy Code

The Fifth Circuit's judgment is in conflict with this Court's decisions establishing that the Federal Rules of Civil Procedure must be applied so as not to impair substantive rights. *See Sibbach v. Wilson & Co.*, 312 U.S. 1, 10 (1941) (Rules must be applied so as neither to "abridge, enlarge, nor modify substantive rights in the guise of regulating procedure") (internal quotations omitted); *see also* 28 U.S.C. §2072(b) ("Such rules shall not abridge, enlarge or modify any substantive right.").

In enacting 11 U.S.C. §105(a), Congress conferred upon bankruptcy courts the substantive power to enjoin any proceeding determined to impair or hinder the debtor's reorganization efforts. The §105(a) stay was intended to protect the substantive rights of Celotex's many creditors and to protect Celotex's reorganization, the results that Chapter 11 was enacted to promote. *See, e.g., NLRB v. Bildisco & Bildisco*, 465 U.S. at 528 ("[t]he fundamental purpose of reorganization is to prevent a debtor from going into liquidation").

If Rule 65.1 is read to authorize execution despite any applicable stay, the rule would directly conflict with an injunction expressly authorized under the Bankruptcy Code. In the event of such a conflict, it is the Federal Rules of Civil Procedure that must invariably give way.

For example, Federal Rule of Civil Procedure 3 provides that a civil action may be commenced "by filing a complaint with the court." Fed. R. Civ. P. 3. However, the Bankruptcy Code's automatic stay provision, 11 U.S.C. §362(a)(1), determines whether and when a civil action may be commenced against an entity that is in bankruptcy. *See Association of St. Croix Condominium Owners v. St. Croix Hotel Corp.*, 682 F.2d 446, 448 (CA3 1982) (automatic stay prohibits commencement of suit against debtor).

Similarly, Federal Rule of Civil Procedure 56(a) provides that a claimant may move for a summary judgment "at any time after the expiration of 20 days from the commencement of the action. . . . " However, where a civil action is pending in federal court against an entity at the time the entity files for bankruptcy, the automatic stay, 11 U.S.C. §362(a), prohibits the debtor's adversary from filing a summary judgment motion. *See Ellis v. Consolidated Diesel Elec. Corp.*, 894 F.2d 371, 373 (CA10 1990).

The various discovery provisions contained in the Federal Rules of Civil Procedure also may not be used against a party that filed for bankruptcy while a federal court civil action was pending. *See Pope v. Manville Forest Prods. Corp.*, 778 F.2d 238, 239 (CA5 1985) ("absent the bankruptcy court's lift of the stay, . . . a case such as the one before us must, as a general rule, simply languish on the court's docket until final disposition of the bankruptcy proceeding").

It is beyond dispute that the §362 automatic stay – an injunction that takes effect without action of the bankruptcy court upon the filing of a petition for bankruptcy – suspends the operation of numerous Federal Rules of Civil Procedure whose operation would conflict with the automatic stay. It follows that where, as here, a bankruptcy court, pursuant to 11 U.S.C. §105(a), issues an injunction to augment the protection afforded the debtor by the automatic stay, that injunction, like the injunction provided by the automatic stay, suspends the operation of those Federal Rules of Civil Procedure which would otherwise permit actions that the injunction prohibits.

Indeed, in a different context, the Second Circuit soundly rejected the argument that a Federal Rule of Civil Procedure can restrict the power of a court to issue an injunction pursuant to 11 U.S.C. §105(a):

> "There is no merit in [appellant's] argument that §105(a) does not apply to the present case on the ground that Fed. R. Bankr. P. 7065 provides that 'Rule 65 F. R. Civ. P. applies in adversary proceedings. . . . ' Rule 65 governs such matters as procedure, notice, time periods, and the proper form and service of injunctive orders. But, like the other Federal Rules of Civil Procedure, *see, e.g., Snyder v. Harris*, 394 U.S. 332, 337-38 (1969) (Rule 23); *Sibbach v. Wilson & Co.*, 312 U.S. 1, 10 (1941) (Rules 35 and 37), Rule 65 may not be construed as a limitation on the jurisdiction or power of the district court to issue a particular kind of injunction. Fed. R. Civ. P. 82." *Green v. Drexler (In re Feit & Drexler, Inc.)*, 760 F.2d 406, 415 (1985).

This is equally true of Rule 65.1.

Accordingly, if this Court were to conclude that enforcement of Rule 65.1 conflicts with enforcement of the bankruptcy court's §105(a) injunction, the Rules Enabling Act, 28 U.S.C. §2072(b), requires that Rule 65.1 give way to enforcement of the bankruptcy court's §105(a) injunction.

Of course, the Edwardses will still be free to seek modification of the §105(a) stay in the bankruptcy court, all the while protected by the supersedeas bond and the reserve account ordered by the bankruptcy court in *Celotex II*. Moreover, the §105(a) stay will be lifted and/or modified when the supersedeas bond adversary proceeding is decided. At that point, the Edwardses either will share in available assets according to the judgment in that proceeding or may use Rule 65.1 to collect the judgment against the surety.

In sum, this Court should hold that Rule 65.1 does not allow the Edwardses to execute upon Celotex's supersedeas bond so long as such execution is prohibited by the §105(a) stay of the Florida bankruptcy court.

III. WHILE THIS COURT SHOULD NOT REACH THE MERITS OF THE §105(a) STAY VIA A COLLATERAL ATTACK, THE BANKRUPTCY COURT DID NOT ABUSE ITS DISCRETION IN ISSUING THE STAY

As described above, this case involves an impermissible collateral attack on the Florida bankruptcy court's §105(a) stay. For this reason, this Court should not address the merits of the stay at this time, just as the Fifth Circuit should not have reviewed the merits.

This point is of particular importance to judicial administration, because the record regarding the §105(a) stay was not before the Texas district court below. The Texas district court held no hearings and received no evidence regarding the §105(a) stay;[13] in contrast, the Florida bankruptcy court held hearings and received voluminous evidence. *Celotex II*, 140 B.R. at 914. Accordingly, the record required for informed appellate review of the §105(a) stay – and for this Court to use in setting standards for the future employment of §105(a) – is where one would expect it to be, in the Florida bankruptcy court.[14]

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[13] This simply illustrates that the Fifth Circuit's decision to review the merits of the stay by collateral attack is bad law and worse policy. The Fifth Circuit disapprovingly noted that materials relevant to a decision to *issue* the §105(a) stay were not before it. *Edwards II*, 6 F.3d at 320 n.7. However, *this very evidence* was in the record before the bankruptcy court. *Compare Edwards II, id., with Celotex II*, 140 B.R. at 914 (discussion of bonds and agreements with sureties placed in evidence). One of the reasons for the rule against collateral attack, of course, is that the court in which the collateral attack occurs does not have the benefit of the full record made in the court which issued the order. That is precisely what happened in this case.

[14] Should the Court wish, Celotex will make that record (which is voluminous) available to the Court.

The power of the bankruptcy court to issue the §105(a) stay has been demonstrated at length in Parts I.A.2.a. and c. of this Argument, and that discussion will not be repeated here. Celotex respectfully refers the Court to that discussion. Below, Celotex will briefly address the propriety of the stay on its merits in the event the Court determines that it is appropriate to review the merits.

Preliminarily, it is important to note that the abuse of discretion standard should be used to review the §105(a) stay. *See Doran v. Salem Inn, Inc.*, 422 U.S. 922, 931-32 (1975) (abuse of discretion standard should be used to review merits of preliminary injunction); *Brown v. Chote*, 411 U.S. 452, 457 (1973) (same); *American Imaging Servs., Inc. v. Eagle-Picher Indus., Inc. (In re Eagle-Picher Indus., Inc.)*, 963 F.2d 855, 858 (CA6 1992) (abuse of discretion standard to be used in reviewing bankruptcy court's §105(a) stay of proceedings against debtor's officers); *Commonwealth Oil Ref. Co. v. United States Envtl. Protection Agency (In re Commonwealth Oil Ref. Co.)*, 805 F.2d 1175, 1188 (CA5 1986) (abuse of discretion standard used to review denial of §105(a) stay), *cert. denied*, 483 U.S. 1005 (1987).[15] In this case, it is beyond dispute that there was no abuse of discretion.

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[15] In *Edwards II*, the Fifth Circuit, in reviewing the advisability of the stay, never addressed the standard of review which it was to employ. To the extent that it was considering an appeal of a collateral attack, the Fifth Circuit should have reviewed the record for the existence of the three collateral attack exceptions which this Court set forth in *Walker, GTE Sylvania* and similar decisions. To the extent that it was reviewing the merits of the §105(a) stay, the Fifth Circuit should have employed the abuse of discretion standard it used in *Commonwealth Oil*.

A. The Bankruptcy Court's §105(a) Stay, Entered To Protect Celotex's Reorganization And All Of Its Creditors, Was Justified

The critical role of Celotex's insurance and the supersedeas bonds in Celotex's bankruptcy case has been explained in detail in the Statement of the Case. The bonded judgments alone represented $70 million of assets otherwise available for creditors on the petition date. The bankruptcy court must determine whether some or all of those assets can be distributed to other creditors as a result of the bankruptcy.

The bankruptcy court's powers to avoid transfers and subordinate or disallow claims – under appropriate factual circumstances – are plain. Transfers of assets related to bonded judgments which fall within the preference period can and should be set aside as preferential. Transfers of assets related to bonded judgments which are constructively fraudulent conveyances (*e.g.*, a transfer on account of punitive damages is not for reasonably equivalent value, since the recipient gave *no* value), can and should be set aside as constructively fraudulent transfers under federal and state law. (The verdict, entry of judgment and posting of the bond in the Edwardses' civil tort action are all within Florida's four year fraudulent conveyance period, Fla. Stat. Ch. 726.110(1)-(2)). Moreover, punitive damage awards can and should be subordinated under 11 U.S.C. §510(c), 11 U.S.C. §726(a)(4) and/or the cases cited in footnote 12 of *Celotex I*. 128 B.R. at 484 n.12. Finally, executory contracts with the sureties can be rejected under 11 U.S.C. §365. As the bankruptcy court held, these debtor-creditor issues should be resolved by the bankruptcy court before the $70 million is distributed.[16] *Celotex I*, 128 B.R. at 484. If Celotex's

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[16] In making this determination, the bankruptcy court employed the proper standard for the grant of injunctive relief.

supersedeas bonds are executed upon, as a practical matter the bankruptcy court will lose its ability to grant effective relief with respect to these issues.

When Celotex and Carey Canada filed for relief in bankruptcy, there were approximately 140,000 asbestos claimants who were not the beneficiaries of supersedeas bonds. *Id.* at 482. As previously noted, these claimants will likely collect only a fraction of their compensatory damages – and no punitive damages. There were also approximately 100 supersedeas bonds, collateralized by nearly $70 million worth of Celotex's assets, *id.*; *Celotex II*, 140 B.R. at 914 (explaining collateralization), posted to benefit 229 judgment claimants. Under these circumstances, as the Fourth Circuit's analysis in *Willis* illustrates, *see* 978 F.2d at 149-50, it is not an abuse of discretion for the bankruptcy court to stay execution on the bonds until it can resolve the issues currently before it for decision. Indeed, faced with these facts, it would be an abuse of discretion *not* to stay execution.

B. The Fifth Circuit's Decision Overlooks The Important Bankruptcy Policies That The §105(a) Stay Promoted

The *Edwards II* decision completely disregards the bankruptcy policy that similarly situated creditors must

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See Celotex II, 140 B.R. at 914-16 (discussing and applying the Eleventh Circuit's four part standard for such relief). Celotex refers the Court to that discussion for the details regarding how the standard is met here. *See id.* Moreover, the Sixth Circuit in *Eagle-Picher* held that, in this context, the bankruptcy court need not even give any significant weight to the factor involving the debtor's ultimate likelihood of success on the merits. 963 F.2d at 859-60. Here, of course, the bankruptcy court found that Celotex made a clear evidentiary showing with regard to this factor, as well as the other three factors. *Celotex II*, 140 B.R. at 914-16. These factual findings are not clearly erroneous and thus cannot be set aside on appeal. Fed. R. Bankr. P. 8013.

be treated alike. *See, e.g., Phoenix Mut. Life Ins. Co. v. Greystone III Joint Venture (In re Greystone III Joint Venture)*, 995 F.2d 1274, 1277 (CA5 1991) (discussing need to treat similarly situated creditors alike), *cert. denied*, 113 S. Ct. 72 (1992). Because the Fifth Circuit improperly allowed a collateral attack to succeed while the Fourth Circuit did not, Celotex's bonded judgment creditors with cases pending in the Fifth Circuit were permitted to recover upon their judgments immediately, while in the Fourth Circuit, bonded judgment creditors were required to seek relief from the Florida bankruptcy court.

Public policy mandates a centralization of authority to govern debtor-creditor relationships in a bankruptcy case. The bankruptcy court must act in the interest of the debtor's reorganization and protect the rights of *all* creditors wherever located. Thus, the bankruptcy court often will view the equities of a given situation differently from a court presiding over an isolated proceeding. The Fifth Circuit concluded, based upon a plainly inadequate record, that the equities favored a ruling that allowed two plaintiffs before it to execute upon a supersedeas bond to collect an award of punitive damages against Celotex. In so doing, the Fifth Circuit made a judgment which the Florida bankruptcy court was better positioned and qualified, as well as exclusively authorized, to make. This judgment must be made with all creditors – not just the Edwardses – in mind.

The *Edwards II* decision also overlooks the fact that the §105(a) stay merely maintains the status quo for a time and does not destroy any rights to the supersedeas bonds. The stay enables the bankruptcy court to determine whether the transfers to procure the bonds can be avoided or the claims subordinated or disallowed. It may also enable the bankruptcy court to confirm a plan of reorganization that may alter or otherwise modify payment obligations as to the affirmed judgments. *See* 11 U.S.C. §1123. Such bankruptcy court actions could permit

the use of Celotex's collateral to benefit all creditors. Finally, the *Edwards II* decision intruded upon the bankruptcy court's exclusive jurisdiction over Celotex's property, the cash that secures Celotex's supersedeas bonds, and the determination of what may constitute property by virtue of the avoiding powers available in a bankruptcy. *See* 28 U.S.C. §1334(d); *see generally United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983).

The bankruptcy court is in the best position to address these complex disputed issues via a full and fair determination on the merits. *See, e.g., Celotex II*, 140 B.R. at 917 (ordering Celotex to initiate an adversary proceeding against the beneficiaries of, and sureties on, supersedeas bonds). The Fifth Circuit's decision attempts to "dispense justice" by divesting the bankruptcy court of its exclusive jurisdiction to make determinations which are *critical* to Celotex's reorganization effort. Indeed, the Fifth Circuit's decision, if affirmed, would ensure that *no court* will address these issues, on the merits, as to the Edwardses.

C. The Edwardses' Expectations Regarding The Supersedeas Bond, While Not Controlling, Have Not Yet Been Disappointed

Instead of acknowledging the many reasons favoring deference to the bankruptcy court's injunctive order, the court in *Edwards II* spoke in poignant terms about its duty to see that the Edwardses' expectations regarding Celotex's supersedeas bond were not dashed. *See Edwards II*, 6 F.3d at 320.

The Edwardses' expectations, while worthy of consideration, simply are not controlling. This Court has recognized that bankruptcy affects the settled expectations of creditors and third-parties alike. *See Whiting Pools*, 462 U.S. at 206 ("As does all bankruptcy law,

§542(a) modifies the procedural rights available to creditors to protect and satisfy their liens."); *NLRB v. Bildisco & Bildisco*, 465 U.S. at 532 ("But the filing of the petition in bankruptcy means that the collective-bargaining agreement is no longer immediately enforceable, and may never be enforceable again."). The postponement of enjoyment, or modification, of the Edwardses' pre-petition "rights" is far from unique in the Celotex bankruptcy or unusual in bankruptcies in general. *See Whiting Pools*, 462 U.S. at 206.

As matters stand today, the Edwardses are in no worse position than the day Celotex filed for bankruptcy. The Florida bankruptcy court's §105(a) stay does not discharge Celotex's supersedeas bond, nor does the stay reduce the amount of the bond. Indeed, in the exercise of its discretion to balance the claims of competing creditors, the bankruptcy court has directed Celotex to establish a reserve account as adequate protection for the bonded claimants, including the Edwardses. *Celotex II*, 140 B.R. at 917. This is an appropriate balancing of the equities.

The exact benefit that the Edwardses will ultimately obtain from Celotex's supersedeas bond has not yet been determined. However, the Edwardses' expectations regarding the bond have not yet been disappointed. The Edwardses have simply been put on hold pending resolution of the important bankruptcy issues implicated here. Meanwhile, their interests have been protected. This is eminently reasonable under difficult circumstances. It is not an abuse of discretion.

Accordingly, in the event that this Court were to conclude that the Fifth Circuit appropriately reached or could reach the merits of the bankruptcy court's §105(a) stay, this Court should hold that the bankruptcy court did not abuse its discretion in issuing its stay.

CONCLUSION

For the foregoing reasons, the judgment of the United States Court of Appeals for the Fifth Circuit should be reversed.

Respectfully submitted,

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